278-192-MSH-jf

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
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Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98

MAY 16 1996

COMMENTS OF TDS TELECOMMUNICATIONS CORPORATION

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May 16, 1996

No. of Copies rec'd 0+16
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Summary

The Act prescribes three levels of interconnection requirements, with the most detailed rules for incumbent LECs, but the law stresses market forces from the outset. The FCC should foster the Act's innovative interconnection framework, which deregulates the terms of voluntary interconnection arrangements negotiated by carriers, subject to limited state review. If negotiations fail to settle all issues, the law then requires state commissions to set the terms via compulsory arbitration. The statutory plan for state arbitration includes pricing standards and more exacting review of arrangements.

The FCC could set minimum standards for unbundling network elements and preventing exclusionary pricing. But negotiations and state arbitration for interconnection arrangements must recognize and accommodate differences in rural telecommunications conditions, the facts of particular requests, and rural LECs' diversity. Congress recognized rural differences, including the availability of relief from interconnection requirements. Rural LECs are exempt from the "incumbent LEC" duties. The state commission may terminate the exemption after a bona fide request to interconnect, if the state rules the request (a) technically feasible, (b) not unduly economically burdensome, and (c) consistent with the Act's specific universal service principles. For all purposes, a bona fide interconnection request should involve a specific commitment to use the requested interconnection and cover its costs. Also under state authority, as the NPRM correctly recognizes, is the duty to grant modification or suspension of all but the most general interconnection requirements if that provision's impact and public interest test are met.

Although the NPRM proposes detailed interconnection and pricing standards, Congress has committed most interconnection determinations to carrier negotiations or state arbitration. The FCC should not adopt most of the uniform nationwide standards it proposes, since flexibility and state experimentation will best foster negotiations and a smooth transition to a competitive marketplace. In particular, the FCC should adopt only the loop, switching, signaling and transport as minimum unbundling elements, leaving the process to work out further details and avoid inefficient network fragmentation. Resale, like unbundling, should allow the providing LEC to recover its costs. Resale of universal services should be at retail rates for exempt carriers, and not discounted below cost under the "wholesale" avoidable cost discount from retail pricing for any LEC. Universal service cost recovery should not be shifted to competing carriers, and adverse customer impact from lost contribution should be avoided.

The FCC should not adopt interconnection pricing standards, especially using the incremental cost proposals the NPRM discusses. The Act's interconnection pricing standard, involving cost and a reasonable profit, requires total cost recovery, including both a share of joint and common costs and embedded costs. Proxies are especially inaccurate for small and rural LECs. And it is crucial to coordinate universal service, access and interconnection decisions and protect customers from rate increases or stagnant network development.

Finally, "reciprocal compensation" for carriers originating and terminating each other's calls requires cost recovery by both carriers. "Symmetry" based on proxies or the incumbent LEC's costs and mandatory bill-and-keep arrangements are inconsistent with the law's mutual cost recovery requirement.

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TDS Telecommunications Corporation (TDS Telecom or TDS), by its attorneys and on behalf of its local exchange carriers (LECs), submits these comments in response to the Commission's April 19, 1996 Notice of Proposed Rulemaking (NPRM), FCC 96-98, in the above- captioned proceeding. The TDS LECs serve 102 primarily rural study areas in 28 states. They have been active in federal and state legislative and regulatory processes seeking to maintain their ability to provide the high quality, evolving, affordable service their rural customers need in today's information economy and society.

The Telecommunications Act of 1996[1] provides the blueprint for a telecommunications marketplace increasingly driven by competition and decreasingly controlled by government regulation. The Act's other paramount policy commitment is to preserve and advance the evolving, nationwide, public switched universal service network that provides a national economic and societal resource of great and growing value. The Act shows that Congress recognizes the importance of rural telephone companies, like the TDS Telecom LECs, in providing modern affordable services in rural areas. The Commission's challenge in this

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[1]Pub. L. No. 104-104. 110 Stat. 56 (1996).

proceeding is to promote competition without impairing the interests of rural customers, as the Act endeavors to do via its numerous accommodations for the differences in rural conditions and the variances among rural LECs.

The 1996 Act Prefers and Encourages Interconnection Under Carrier-Negotiated Agreements
[NPRM Sections IIA(2), IIB(1), and III]

The 1996 Act offers local exchange carriers and their competitors the option of avoiding regulation of their interconnection arrangements almost entirely if they can agree on interconnection terms. The legislation provides three layers of requirements, graduated in the degree of regulatory burden and detail by the type of carrier involved. From two general requirements for all telecommunications carriers,[2] the list increases to five basic requirements for all local exchange providers,[3] and a still more detailed list for incumbent LECs.[4] When carriers cannot fully agree, the Act defers to any agreed-upon terms that have emerged from voluntary negotiation, and commits to the states the task of mediating voluntary agreements or, if necessary, securing interconnection agreements through compulsory arbitration.[5]

As a backup for the opportunity to achieve a totally deregulatory, marketplace-controlled interconnection regime via negotiations, the Act provides specific requirements and standards that will govern arbitrated arrangements until negotiation can become the rule. All telecommunications carriers must interconnect and comply with interoperability standards. All

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[2] § 251(a).

[3] § 251(b).

[4] § 251(c).

[5] § 252.

local exchange carriers must meet general requirements for resale, number portability, dialing parity, access to rights of way and reciprocal compensation for the transport and termination of telecommunications. Incumbent LECs also have the more detailed obligations to (1) negotiate in good faith, (2) interconnect reasonably, equally and without discrimination, (3) unbundle their network elements, (4) resell their retail services at wholesale rates, (5) provide notice of changes, and (6) generally allow physical collocation.

Notwithstanding the Commission's apparent concern (¶ 31) that rules are necessary to correct for the "effect of the incumbent's bargaining power on the outcome of the negotiations," the structure chosen by Congress actually puts the strongest pressure to agree to voluntary terms upon the incumbent. Failure to agree assures that it will have substantially greater regulatory burdens imposed in arbitration than its requesting, largely unregulated competitor. In any event, the requesting carrier can always demand enforcement of the statutory requirements by simply refusing to agree to proffered terms. The concept of free market bargaining as the negotiating "carrot" and state-tailored terms and conditions under statutory standards as the regulatory "stick" represents the Act's innovative, carefully counterbalanced experiment in transitioning to competition. The Commission should not throw the Act's transition mechanism out of adjustment.

At most, the FCC should establish minimum standards for unbundling network elements and prevention of exclusionary pricing. Particular interconnection requests will occur under diverse market conditions, however. Thus, any FCC rules should allow broad discretion for reasonable negotiation and state commission decisions based on specific facts.

Owing to the diversity of rural LECs, burdensome and unreasonable nationwide rules are potentially most harmful in their markets.

The Interconnection Blueprint for Rural Telephone Companies
Reflects the Act's Policy of Accommodating Rural Differences
[NPRM Section IIF]

The interconnection framework Congress has devised for rural telephone companies[6] follows the wisdom of the Act's overall pattern: It recognizes the different and varied needs and concerns of rural areas and accommodates them with flexible, tailored approaches. Accordingly, Section 251(f) provides that, at least initially, virtually all rural telephone companies will be exempt from the interconnection requirements that Section 251(c) imposes on all other incumbent telephone companies. Rural LECs are subject to the five duties in Section 251(b) that apply to all LECs, as described above. Under the "rebuttable" Section 251(f)(1) exemption, rural LECs need not: negotiate with requesting carriers, meet the stricter incumbent LECs' interconnection requirements in subsection (c)(2), provide unbundled network elements under subsection (c)(3), provide their retail services at wholesale rates to other carriers, give notice of changes affecting interoperability under subsection (c)(5) or provide physical or virtual collocation under subsection(c)(6).

The state must examine the rural LEC exemption in an expedited proceeding when the LEC receives a bona fide request for interconnection. The state will terminate the exemption only if it finds that the requested interconnection "is not unduly economically burdensome, is

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[6]TDS will use the term "rural LEC" hereafter for carriers that fall within the definition of "rural telephone company" in Section 3(47) of the Communications Act, as amended.

technically feasible, and is consistent with the six specific universal service principles in Section 254."[7]

The Commission Should Define "Bona Fide Request" Consistent With a Binding Carrier Commitment to Use the Requested Interconnection [NPRM Sections IIA-B and F]

The concept of a bona fide request is central to the rural exemption. It also has significance in the application of all the interconnection requirements and standards in subsections 251(b) and (c). Specificity is important in the interconnection framework designed to promote customized, market-fact driven interconnections. As the conferees express it (Managers' Statement at 123):

> The duties imposed under new section 251 (b) make sense only in the context of a specific request from another telecommunications carrier or any other person who actually seeks to connect with or provide services using the LEC's network. [8]

Real demand and not hypothetical, tentative or blanket requests are essential. The expense of having to put into effect any of the requirements in Section 251 or 252 without a commitment that at least one carrier will actually use the interconnection and the interconnector will pay its cost would be particularly onerous for rural LECs, given their typically low density and consequent high unit cost of providing almost any service, facility or function.

A bona fide request should meet the responding carrier's need for adequate information and commitment and prevent a requesting carrier from making blanket or premature requests

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[7]Section 251(f)(1)(B)-(C).

[8]The Act also refers frequently to a requesting carrier in the incumbent LEC duties enumerated in subsection 251 (c).

for interconnection. Since they are able to obtain government-enforced interconnection if voluntary negotiation fails, requesting carriers should shoulder the responsibility for starting the statutory interconnection process only with firm, enforceable orders for particular arrangements.

TDS Telecom understands that USTA advocates a requirement that any requesting carrier must offer service using the requested interconnection within one year and commit itself to taking at least one year of service. Its recommended policy would also require that the request identify the points and dates of interconnection. USTA also urges the standard that a request would enable the responding LEC to recover its investments and expenses for the requested interconnection. TDS Telecom endorses these attributes as requirements for a bona fide request for any interconnection purpose.

As the NPRM tentatively recognizes (¶ 261), rural LEC interconnection exemption determinations are solely the province of the states. TDS agrees that the Commission should not impose further mandatory requirements on the states regarding their duties under Section 251(f)(1).

The Commission Is Also Right to Defer to the States on Modifications and Suspensions [NPRM Section IIF]

The Act's flexible safeguards for rural LEC interconnection duties do not stop with the exemption. At any point, a rural LEC or any other LEC with less than 2% of the nation's aggregate access lines is entitled to petition its state under subsection 251(f)(2) for suspension or modification of any or all of the interconnection requirements imposed on all LECs or

incumbent LECs by subsections 251(b) and (c), respectively. The state "shall" grant a requested suspension or modification, says the Act, "to the extent that, and for such duration ..." as the state finds necessary to avoid a significant adverse impact on customers or an "unduly economically burdensome" or "technically infeasible" requirement, provided that the modification or suspension is also "consistent with the public interest."

These standards and procedures for relieving small and rural LECs from the interconnection provisions described above are clearly spelled out in the law. Thus, there is no need for Commission action. Like the exemption provisions, they evidence the Act's recognition that, for areas served by rural and small LECs, it cannot be presumed that pro-competitive measures designed for larger LECs and more densely populated areas will be suitable where market conditions are different.[9] The Commission need only incorporate the specific provisions in subsection 251(f) in its rules.

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[9]The Commission has, in the past, frequently refrained from applying the full weight of its regulations to small and rural LECs because of their diversity, divergent market conditions, lack of national market power and other significant differences. Different treatment for small and rural LECs has been Commission policy with respect to requirements ranging from ONA and CEI requirements (see, Computer III Remand Proceedings, 6 FCC Rcd 174 (1990), ordering expanded interconnection (see, Rules Section 64.1401-1402), and forgoing mandatory price caps regulation, Policy and Rules Concerning Rates for Dominant Carriers, 5 FCC Rcd 6786, 6837 (1990) to retaining the ability of small and mid-sized LECs to pool and participate in joint access tariffs MTS and WATS Market Structure, CC docket Nos. 78-72 and 80-286, 2 FCC Rcd 2953 (1987). It is likely that Congress intended the FCC to continue to implement its rules in a way that recognizes the diversity and unique characteristics of rural LECs.

The Commission Should Be Cognizant of Rural Differences in Its Overall Implementation of Interconnection

[NPRM Sections IIA, B, C, F, and III]

Congress has emulated the Commission's established policy of tailoring relief and policy for rural and small LECs in the 1996 Act. Indeed, it has made a cluster of rural safeguards available. These include: the "rural markets" provision that allows states to limit competition in rural LEC study areas to non-creamskimming, area-wide universal service, Section 253 (f); the requirement that states must make a public interest finding before they designate any additional eligible carrier to participate in universal service cost recovery mechanisms in a rural LEC's service area, Section 214(e); the opportunity for "infrastructure sharing" with larger LECs , Section 259; and some increased flexibility to integrate cable and telephone operations in rural areas (Section 652).

The NPRM correctly recognizes that Congress chose to customize interconnection requirements and the transition to local competition for its rural LEC study areas. The underlying rationale for all of the Commission precedents and 1996 Act provisions for rural LEC study areas is the same -- the need to take rural differences into account in framing and implementing public policy. Congress has now recognized that state-by-state scrutiny is the best way to accomplish locality-specific rural tailoring for interconnection and most other purposes. Consequently, it is essential that the Commission maintain its tentative conclusion to accord states the discretion and flexibility enacted by Congress and acknowledged by the NPRM.

The Overall Interconnection Model for Incumbent and Other LECs Also Imposes Regulation Primarily by the States, and Only If Deregulated Interconnection Negotiations Fail
[NPRM Sections IIA-C, and III]

The rural and small LEC exemption, modification and suspension provisions represent a sound public policy tool to prevent interconnection requirements designed for denser markets from adversely affecting many rural customers and incumbent LECs. However, exemptions and modifications cannot be expected to resolve all the tensions between the Act's interconnection requirements and the needs of rural customers and carriers, now or in the future as rural markets develop and mature. Therefore, implementation of the Act's full menu of interconnection requirements for all LECs (under § 251(b)) and for incumbent LECs (under § 251(c)) is important to rural LECs as well as to larger, more urban LECs.

As noted, the interconnection model crafted by the conferees encourages voluntary carrier negotiations and moves on to compulsory state arbitration -- and the statutory, state and limited FCC standards arbitration brings to the process under Section 252 -- only when the less regulatory means have failed. The standards for state review of agreements also become stricter if the carriers cannot agree. State review of successfully negotiated interconnection arrangements is limited to rejecting an agreement if it discriminates against a non-party or is not in the public interest. (Sec. 252 (e)(2)(A)(i)-(ii)). If the carriers cannot agree, they may seek state commission mediation. Again, the aim is to reach a mutually agreeable interconnection arrangement, which will be reviewed under the same minimally intrusive standards as a fully negotiated agreement or the successfully negotiated portions of a partially arbitrated arrangement. (Section 252(e)(2)).

The genius of the Act's negotiation and mediation provisions is that they let the marketplace begin to operate as soon as possible, even before competition is fully established. But a requesting carrier that cannot obtain an acceptable bargain in such a marketplace-like setting can invoke regulatory help by requesting compulsory state commission arbitration for unsettled issues. The ensuing arbitration process under Section 252 requires the state to enforce compliance with the statutory interconnection requirements set forth in Section 251. The state must also enforce "the regulations prescribed by the Commission pursuant to Section 251." (Section 252 (c))(emphasis added). Section 252(c)(2) also imposes a separate standard for state arbitration, by authorizing and requiring the state to "establish any rates for interconnection, services, or network elements according to subsection [252] (d)." Consulting Section 251 to determine which regulations the Commission is called upon to "prescribe[]...pursuant to Section 251," we find that the Commission's rulemaking responsibility is carefully spelled out -- and quite limited. Where Congress intends the Commission to act, the statute is specific. Hence, it is reasonable to conclude that Commission regulation is not intended when Congress has not so stated in the Act. It is significant, given this Congressional specificity, that the statute's authorization of Commission regulations includes only the following short list: (1) prescribing number portability requirements (Sec. 251(d)(2)); (2) taking "actions necessary to establish regulations to implement the requirements of this section" (Sec. 251(d)(1))(emphasis added); (3) determining "what network elements should be made available" for purposes of the subsection (c)(3) unbundling duty (Sec. 251 (d)(2)); (4) supervising numbering administration (Sec. 251(e)); (5)

designating additional "incumbent carriers" (Sec. 251(h)(2));[10] and (6) continuing to exercise its longstanding jurisdiction under Section 201, (Sec. 251 (i)). Subsection 251(d)(3) also explicitly forbids the Commission to interfere with state requirements for access or interconnection that do not either frustrate implementation or conflict with Section 251.

The limits on the FCC's authority and the evident Congressional intent to assure adequate state authority are key elements in the two interconnection sections. Section 252 does not give the Commission any additional rulemaking responsibilities or authority to interpret, limit or steer carrier negotiations or state arbitration. Indeed, the role it assigns to the state commissions in arbitrating and reviewing carrier agreements and BOC statements of generally available terms and conditions effectively leaves the Commission to exercise only the specific and limited, albeit crucial, powers expressly conferred by Section 251.

The Act Calls for State Experimentation, Not Federal Regimentation of Interconnection Standards
[NPRM Sections IIA-B, and III]

The NPRM envisions a far larger role for the Commission than the Act authorizes. For example, the Commission proposes a number of national standards to ensure uniformity among the states and to help competitors to compete in multiple jurisdictions.[11] Among the

[10]With regard to this statutorily-assigned Commission power, TDS Telecom urges the Commission to develop a test for designating additional "incumbent carriers" that will assign the same level of interconnection requirements to all carriers that offer competitive local exchange and exchange access services in the same area. Negotiations will be increasingly more likely to succeed if competitors in an incumbent LEC's service area do not have the incentive to invoke the arbitration process as a way to impose the maximum level of asymmetrical regulation on the original "incumbent" universal service provider.

[11]NPRM at ¶¶ 25-36.

Commission's reasons for proposing expansive federal standards are its desire to narrow the options available to negotiating carriers and to force states to heed FCC-imposed parameters in exercising their arbitration and review powers. The Commission also undertakes to compare state rules and policies and endorse some, but possibly even condemn others.[12]

The rules and standards the Commission is planning to impose almost across-the-board would interfere with the statutory negotiation process by leaving fewer choices that might secure both parties' voluntary agreement. Extensive federal rules and standards would also interfere with the Act's reliance on states to make interconnection decisions, presumably because states are more likely to know or discover the specific market facts surrounding particular interconnection requests. Greater Commission control of the results of negotiation and arbitration alike could also drive more parties to seek waivers under the modification and suspension section. With less federal regulation, more carriers might find enough flexibility in the arbitration process to forgo waiver requests and move more quickly towards market-driven agreements. Finally, by constraining the operation of market forces and the implementation choices of the states, the Commission will impede the diverse experimentation by different states which could develop further innovative transition arrangements to move towards fully competitive markets.[13]

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[12]See, e.g., ¶¶ 52, 59, 62, 82 (seeking comments on state policies that have merit or may conflict with the Act's purposes, as the Commission views them).

[13]The NPRM demonstrates the Commission's interest in how various states are dealing with various interconnection issues, since it repeatedly seeks input on the outcome of state initiatives. However, Congress has taken no action that could indicate its intention or acquiescence in the Commission's plan to choose which state approaches to anoint as national policy.

Entrusting the detailed implementation of the interconnection provisions to the individual states -- echoing the Act's other state-administered rural safeguards -- brings into prominence both the state commissions' typical familiarity with local conditions and their more direct accountability to the consumers and businesses affected by their decisions. For rural areas, this local sensitivity can spell the difference between the ability to discern what is harmful or beneficial for the public, what is technically and economically feasible and what is optimal public policy.

The Commission Should Require Only a Minimum Set of Unbundled Network Elements
[NPRM Section IIB(2)(c)]

The Act explicitly authorizes Commission rules to define what network elements should be made available to satisfy the incumbent LEC requirement to provide unbundled elements at any technically feasible point. The Commission is weighing (¶ 92) whether to identify only a few elements as nationwide requirements or to prescribe further fragmentation of network functions to help competitors operate a network without building all such components. The proposal to identify only a few "minimum" network elements as national unbundling requirements is consistent with the competitively neutral outlook the NPRM espouses. (¶ 11). The proposal is flexible, which is beneficial in that it will leave the states room to tailor any additional unbundling requirements to particular requests and market conditions and to respond to future changes in those conditions.

The basic elements this Commission specifies should include the local loop, switching, signaling and related databases and transport links. Instead of developing more detailed

standards for acceptable unbundling points and terms, or further proliferating the bits and pieces about which bargaining must take place, the Commission should let the innovative statutory negotiation and arbitration process play the major role in further refining unbundled components. The Commission should not try to control prices for unbundled network elements. Price negotiations are likely to be the subject of brisk negotiation, reflecting local market conditions, which is just the kind of marketplace force the Act's interconnection structure seeks to encourage. The FCC could establish ceilings to prevent exclusionary pricing, as long as they were based on total embedded stand-alone costs.

A more detailed federal definition of unbundled elements will actually thwart competition by failing to take into account the myriad of network topologies deployed today. Given the varied network architectures, negotiations will likely require analysis of how and where interconnection will occur. Business goals and detailed network implementation will need to be coordinated. Rigid network standards in national rules could force incumbents in directions that would not be optimal, such as not introducing newer, more elegant technologies that could not conform to the rigid network standards their competitors are not required to meet.

The Commission, therefore, will be instrumental in balancing the impact of disaggregating LEC networks that were designed to provide retail services to end-users to make available artificial components to be incorporated in other carriers' networks. It will be of paramount importance for the Commission to abide by (a) its recognition (¶¶ 11-12) that Congress did not intend "to divest incumbent LECs of all or part of their local networks" or

prevent their earning "a reasonable profit for the interconnection services" and (2) its endorsement that the goal is "not to ensure that entry shall take place irrespective of costs."

The Commission should, however, clarify the distinction between unbundled network elements and services available for resale. The notion that unbundling and resale are interchangeable or overlapping concepts must be laid to rest. A LEC that is required to offer unbundled elements must be able to recover its costs, including a reasonable profit. It should not have to provide fractional components without a binding agreement that an actual requesting carrier will use and pay for the elements. The Commission should not try to relate the cost of unbundled network elements to the retail or "wholesale" rates for services required to be available for resale by Section 251 (c)(4). They involve different types of interconnection which cannot reasonably be compared.

Unbundling results in inefficiencies in the network by adding to the unused capacity of the underlying carrier and undermining the economies of scope and scale available from the most intensive use of facilities and functions. There is no valid public policy rationale for enabling carriers to use resale and/or unbundled elements to exploit the anomalies of artificial, government-imposed interconnection pricing structures. Indeed, preventing manipulation of the transitional tools for developing competition where it is feasible provides an additional reason both to apply the same resale and unbundling requirements to all market competitors and to allow any carrier to challenge requested interconnection that would require it to provide below-cost service to a competitor.

The Resale Pricing Requirements Should Not Shift Ratepayers' High Cost Support to Competing Carriers
[NPRM Sections IIB(3), and C(1)]

Under Section 251(b)(1), the Act does not impose a pricing standard. It prohibits "unreasonable or discriminatory conditions or limitations" on resale. The impact on universal service cost recovery is a valid consideration for the LEC in setting its resale prices. It would not be unreasonable, for example, for the LEC to charge its retail rates to a reseller. The reseller would not obtain high cost recovery because the LEC's retail rates would already reflect its high cost support.

The wholesale and retail cost requirements of Section 251(c)(4) are among the issues committed to carrier negotiations and state arbitration. Resale rates must be sufficient for the incumbent LEC to recover its costs. The FCC should also adopt a rule for Section 251(c) that a LEC which charges retail rates that reflect federal high cost recovery not be required to sell at a further discount from its below-cost retail rates. Otherwise, the federal high cost programs intended to keep rates reasonable and affordable for customers will instead flow to the bottom line of competitors or fuel unfair competition by resellers that enjoy, in effect, a double discount and the resulting unfair competitive advantage.

The Commission Should Not Adopt Proposed Pricing Standards for Interconnection, Especially for Rural LECs
[NPRM Sections IB, IIB and III]

The NPRM (¶ 117 et seq.) discusses a series of pricing standards and cost methodologies that the Commission has under consideration as uniform national requirements for purposes of interconnection. The notion is that the Commission shares authority over

pricing issues with the states, which will be required to apply pricing and cost standards in the arbitration process. The NPRM would have the FCC interpret and apply the statutory standard that requires pricing for interconnection to reflect the underlying cost of network elements, Sec. 252 (d)(1).

As the earlier discussion of the statutory division of authority demonstrates, Congress has not given the Commission authority to control interconnection pricing or cost methodologies.[14] Not only is the Act silent about such authority for the FCC, but the basic structure of carrier negotiations, backed up by state arbitration, is at odds with Commission micromanagement. This structure in itself calls into serious question the FCC's keen interest (¶ 119) in preventing state variations in pricing that reflect differences in the market-facts.

The Act Does Not Prevent Investment and Expense Based Cost Recovery
[NPRM Section IIB(2)(d)]

The Act requires that interconnection and network element charges be cost-based, and may "include a reasonable profit," but must not be developed in a "rate-of-return or other cost-based proceeding." The NPRM (¶ 123) interprets this to preclude states from using traditional historical costs and rate base information. It goes on to claim (ibid) that this pricing standard also requires the use of forward-looking costs.

The NPRM's obituary for rate-of-return regulation is probably premature. The conferees deliberately eliminated language from the bills under discussion during the

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[14]This and the other statutory pricing standards that the Commission plans to particularize in regulations actually provide further illustration of the Commission's lack of authority to do so: The standards come from Section 252, which enacted them for the purpose of state arbitration determinations.

conference that would have outlawed rate-of-return regulation.[15] Hence, it seems the Commission is attaching too much weight to this supposed consequence of the cost-based pricing requirement. Indeed, the incremental price measures the NPRM goes on to discuss would likely prevent LECs from recovering their embedded costs of service and joint and common costs, thereby precluding a "reasonable profit,"and would discourage future infrastructure investment incentives. TDS suggests that the better reading of the rate-of-return caveat in Section 252(d)(1)(A) is that Congress wanted to provide adequate compensation for forced LEC interconnection arrangements, but wanted to avoid imposing the cost and burden of "a rate-of-return proceeding (emphasis added)," the precise phrase it chose to express its intention.

LRIC- and TSLRIC-Based Rates Violate the Statutory Standard
[NPRM Sections IIB(2)(d), and III]

Although the NPRM recognizes some of the difficulties with using incremental cost measures, it appears (¶¶ 124, 126) to be influenced by the support of some proponents. The problem with LRIC is that it does not take into account either joint and common costs or embedded costs. Imposing a ceiling based on incremental costs in an industry with economies of scale and scope means that LECs will not recover their total costs because their incremental

[15]Telecommunications Conference Staff Recommendations for Resolution of Issues, p. 2 (December 12, 1995). The staff's recommendation to eliminate Senate and House bill provisions to "abolish rate-of-return regulation" was adopted by the conferees in a public meeting.

costs are lower than their average costs.[16] The TSLRIC fiction of isolating the costs of providing one service on its own does not recover real-life costs either. Cost-based recovery must include a share of joint and common costs. Moreover, the Washington Commission has recognized that direct allocation of common costs to particular services to solve the dilemma of recovering for shared costs is not a viable alternative. As it explained the problem, "[s]ince the loop is required ... to provide any one of toll service, access service, or local service, it is incremental to none of the services."[17]

Fundamental fairness, adequate compensation for the past prudent investments of a utility and the need to attract capital to evolve the public switched network counsel against mandating only incremental cost recovery for interconnection a LEC is forced to provide. The "reasonable profit," the state may build into interconnection should take into account the LEC's total cost (including some contribution to joint and common costs) if the state seeks to fulfill the Act's advanced infrastructure incentives commitment[18] and fulfill the LEC's reasonable reliance on the "social compact" underlying public utility investment in the past.

As discussed above (n. 9), the Commission has long been careful to avoid overburdening small and rural LECs with complex and costly requirements designed for larger

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[16]See, J. Panzar, "The Continuing Role for Franchise Monopoly," pp. 7-9 (March 21, 1987).

[17]Washington Utilities and Transportation Commission, Fifteenth Supplemental Order, Docket No. UT-950200, p. 83 (released April 11, 1996).

[18]See, e.g., Sec. 706(a).

LECs. TSLRIC involves burdens that are inappropriate for rural LECs. For any cost measurement use, TSLRIC would require substantial adjustments.

TDS Telecom urges the Commission not to adopt a standard for rural LEC interconnection rates that sets a ceiling on the basis of inadequate incremental cost methods. At most, these measures offer a floor to show that rates are not predatory. Instead, the Commission should use total costs, perhaps based on current access charge calculations, during the transition period and at least until it finishes redesigning the current federal universal service cost mechanisms. The NPRM asks (¶ 145) about including universal service costs in rates for interconnection. It is clearly essential for the Commission to coordinate its interconnection, universal service and access restructure proceedings. Rural universal service cost recovery must remain at adequate levels to prevent higher local rates, inadequate and confiscatory compensation and diminished incentives for network development for rural LECs, or both.

TDS also questions the Commission's rejection (¶ 147) of the Efficient Component Pricing (ECP) concepts, which were advocated by Professors Panzar and Wildman as useful for pricing rural LEC services.[19] In areas with only one eligible telecommunications carrier, the NPRM does not appear to question the logic of ECP. Although TDS agrees that opportunity costs may be hard to calculate, the method should at least be considered as a

[19]J. Panzar and S. Wildman, Competition in the Local Exchange: Appropriate Policies to Maintain Universal Service in Rural Areas, pp. 31-33, 47-48, Appendix D (1995)..